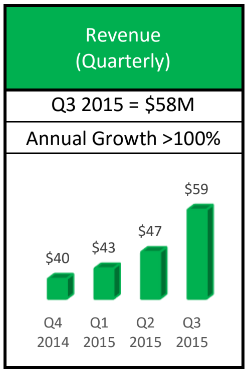
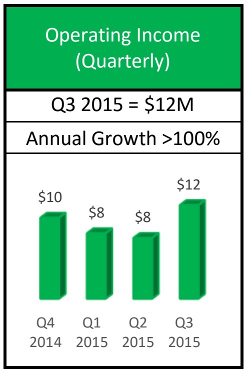
SELECTIVE
WEALTH MANAGEMENT

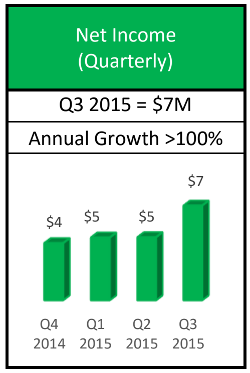
Patriot National
December 18, 2015

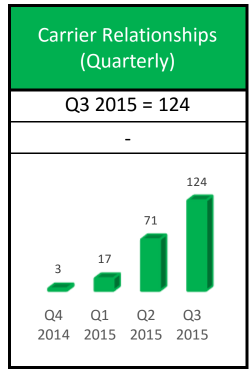
General Overview

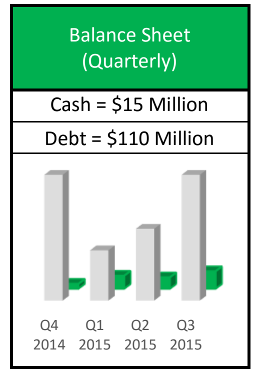
Patriot National (PN) provides outsourcing services for the insurance marketplace. The company specializes in claims administration, adjudication, cost containment, underwriting, and brokerage services. PN was originally a subsidiary of Guarantee Insurance and provided all the administrative functions required to run Guarantee's workers compensation insurance lines. In 2013 the company was spun off from Guarantee and then went public in January 2015. Steven Mariano, the President and CEO, owns 51% of the company and has a long history of successfully building outstanding companies. In the last twelve months the firm has more than doubled revenue, EBITDA, net income, cash flow, and insurance carrier clients. With revenue retention rates in excess of 98% PN has a predictable business model with strong prospects for growth.











Purchase Logic

On December 13, 2015 PN was three weeks away from completing a sensational year. The company acquired 16 businesses, expanded carrier client relationships from 14 to 124, and was targeting $31 million in net income during 2016. With 27 million shares outstanding for $13.00 per share the total market capitalization of the business was just over $350 million dollars or 11.5x forward looking earnings – a fair price for a rapidly growing business.

The following day the company filed a press release indicating that the company would be selling $20 million dollars of stock and Mr. Mariano would be personally selling $30 million dollars of stock at a price of $12 per share (a discount to the prevailing market price of $13). This discount was provided to the institutional buyers for purchasing such a large block of stock and alleviating the pressure that selling such a large volume of shares would cause to a relatively illiquid security. After the private placement there were a total of 29.5 million shares outstanding and the company had raised an additional $20 million in cash. With the additional $20 million in cash the company would have logically been worth $350 million (the price the previous day) + $20 million (the new cash raised) for a share price of $12.54. However, following the announcement the stock plummeted 50% to $6.50 and the company was traded for 6.5x forward looking earnings – a truly sensational price for such an outstanding business. During the chaos we loaded up on shares at an average price of $7.76. The dramatic decline in price was attributed to Mr. Mariano selling $30 million of stock personally, but we believe this was blown way out of proportion. After the sale Mr. Mariano continues to own 51% of the company and has an employment contract as CEO and President that extends until January 2018. His total compensation as CEO is $1 per year. He still owns more than 14 million shares and his success is tied to the success of the shareholders. After the sharp decline in price he publically announced that he would not be selling any additional shares during 2016 and that forward looking guidance remains unchanged. We believe Mr. Mariano's personal sale of stock created an amazing buying opportunity and that PN could likely double in the next 12 months.

Key Metrics

The key metrics that drive success for PN are revenue, carrier relationships, carrier concentration, operating income, balance sheet, and net income. The business factors that drive each of these key metrics are described in further detail below.

Revenue

Revenue is generated by charging insurance carriers fees based on services provided. The services provided include claims administration, adjudication, cost containment, underwriting, and brokerage services. Insurance carriers can partner with PN to provide one service, multiple services, or have PN provide all administrative functions required to run an insurance operation. As an outsourcing partner PN does not assume any insurance risk. The company targets smaller insurance companies, reinsurance captives, and institutions that self-insure. These smaller insurance players don't have the scale required to perform all the administrative aspects of running an insurance operation at the same price point as larger players. Under these circumstances PN is able to provide services at scale for multiple insurance carrier clients simultaneously which saves costs for their clients. Revenue is sticky due to the long-term nature of client relationships with many lasting more than a decade. In the last twelve months Revenue has more than doubled and we anticipate more than 30% growth in 2016. It is very likely that the company will average more than 10% revenue growth for the next 10 years as they sign on additional carrier clients and cross-sell service functions into their existing client base.

Carrier Relationships

A carrier relationship is an insurance company that utilizes at least one of PN's outsourcing services. Carrier relationships are categorized as unbundled, bundled, or turn-key. Unbundled carriers utilize only one of PN services, bundled carriers utilize more than one, and turn-key carrier partners have hired PN to perform all administrative functions. Two years ago PN was a subsidiary of Guarantee Insurance, which is wholly owned by Steven Mariano, the company's CEO. PN had only two primary insurance carrier clients – Guarantee Insurance and Zurich. In 2014 Steven Mariano decided to spin off PN and begin offering outsourcing solutions for more insurance companies. The company was large, well run, and providing substantial cost savings to Guarantee Insurance and Zurich when it went public in 2015. Since that time PN has exploded into the market place signing up 122 new insurance carrier partners. We anticipate PN to continue to rapidly expand the number of carrier partners as well as cross-sell more services to existing clients. We anticipate growth of 20 to 30 carriers per year for the next 5 years.

Carrier Concentration

In 2013 PN operated with essentially 2 primary insurance carriers that generated nearly 100% of revenues. These two carriers were Guarantee Insurance (71%) and Zurich (18%). Obviously the loss of Guarantee or Zurich in 2013 would have been devastating to the business, but Guarantee Insurance is 100% owned by Steven Mariano – the CEO and president of PN. We viewed losing this contract as an impossibility since Steven has more than $100 million dollars of his net worth in PN. Since going public PN has been focused on expanding the number of carrier relationships and reducing the concentration risk of any single carrier, including Guarantee Insurance, to less than 15% of revenue. With the addition of 122 new carriers in 2015 Guarantee Insurance will likely represent approximately 30% of revenue in 2016 due to the increased size of the business and a modest reduction in revenue generated from Guarantee. The company targets less than 15% concentration from any single carrier by the end of 2017. In order to accomplish this feat revenue would have to more than double from the current run-rate. It is our expectation that by the end of 2017 no single carrier would contribute more than 15% of revenues or 15% of net income. In the mean time we view this high level of concentration as low risk due to the fact that Steven Mariano owns 100% of the largest carrier client for PN.

Operating Income

The operating income for PN represents the cash generating capabilities of the business in a 'normal' year before investment gains, interest payments, and taxes. To calculate operating income we took the net income and added back interest payments, depreciation, acquisition related expenses, amortization, and taxes. We view this as a more important metric for monitoring the progress of the business than the net income because PN has a relatively high depreciation and amortization expense due to the highly acquisitive nature of the company. These amortization expenses are largely phantom expenses and don't impact the economic earnings of the company. In the last twelve months the operating income was $38 million dollars. We anticipate this figure to exceed $50 million dollars in 2016 and continue to grow at a rate of roughly 10% for the next 10 years as new carrier relationships are added and existing carriers expand their business with PN. Our purchase price relative to the earning power of the business was sensational.

Balance Sheet

Since the IPO in January PN has acquired 16 companies using credit facilities provided by a banking syndicate. Through this acquisition phase the debt of the company has increased to $110 million compared to $15 million in cash for the business. Prior to our purchase the company announced a secondary offering that raised an additional $20 million dollars increasing the cash portion to $35 million dollars. The company is required to maintain a Debt to EBITDA ratio below 3x under the current credit facility. During 2016 we expect this ratio to be less than 2x and would like to see the company de-lever as the acquisitions are fully integrated into the business. Over the next 10 years we would anticipate the company to maintain an average Debt to EBITDA ratio of approximately 2x.

Summary of Key Metrics

Metric	Expectations
Revenue	Growth of >30% in 2016 Average of 10% over 10 years
Carrier Relationships	Growth of 20 to 30 carriers per year
Carrier Concentration	Less than 15% for the largest carrier
Operating Income	More than $50 million in operating income for 2016 Average of 10% over 10 years
Balance Sheet	Debt to EBITDA of 2x

The Moat Around The Metrics

PN has a competitive moat as a low cost provider, high switching costs, and outstanding management. As an outsourcing service provider with more than 1,000 experienced employee's PN is able to provide administrative functions for small insurance carriers, reinsurance captives, and self-insured entities at a price point that is below what could be achieved performing these same functions in-house. PN has been able to rapidly expand the number of insurance carriers by targeting this niche market and offering substantial cost savings to customers. Additionally, once PN becomes an outsourcing partner of choice the company can maintain that relationship for many years. Customer relationships and carrier partnerships are typically amortized over a 10-year period – demonstrating the long lasting value of these arrangements. Further strengthening the competitive moat is the managerial capabilities of Steven Mariano. With more than 25 years of experience Mr. Mariano has made over $500 million dollars building businesses in the insurance sector. As manager and CEO of this relatively new public entity we see an opportunity for Mr. Mariano to utilize his experience and connections to rapidly expand the client base faster than a typical insurance outsourcing provider. As PN targets smaller insurance operations we believe that Mr. Mariano is an all-start player dominating this untapped minor league market.

Risks

PN is a low risk investment with an exceptionally stable business model. The biggest risk factors are the carrier concentration, high levels of debt, and potential to lose Mr. Mariano. If PN were to lose a contract with one of its major insurance carriers it would have a material impact on the business – particularly Guarantee Insurance which represents 66% of the business. We view this risk as remote due to the 100% ownership stake Mr. Mariano has in Guarantee Insurance and 51% ownership of PN. However, in the event that something were to happen to Mr. Mariano it could potentially put the Guarantee Insurance contract at risk. The company also has relatively high level of debt with a Debt to EBITDA ratio of 2.7x. The $20 million dollar secondary offering recently completed coupled with strong organic growth in the underlying business should reduce this ratio to well below 2.0x during 2016. We view the risk of defaulting on the debt covenant as remote. Last, but not least, the biggest risk we face is if something were to happen to Mr. Mariano. As a key man to the business his knowledge, industry expertise, contacts, and control of Guarantee Insurance are critical to the success of PN. If something were to happen to Mr. Mariano it could put PN it a precarious situation. We do believe that at current prices if Mr. Mariano were unable to resume his role as CEO and President that PN would be successful as an investment.

Conclusion

PN provides outsourcing services for the insurance marketplace. The company specializes in claims administration, adjudication, cost containment, underwriting, and brokerage services. Steven Mariano, the President and CEO, owns 51% of the company and has a long history of successfully building outstanding companies. In the last twelve months the firm has more than doubled revenue, EBITDA, net income, cash flow, and insurance carrier clients. With revenue retention rates in excess of 98% PN has a predictable business model with strong prospects for growth. We were able to opportunistically purchase PN after Mr. Mariano sold $30 million dollars at $12.00 per share. This sale caused the price of the stock to decline from $13.00 per share down to $6.50 per share in two days. We will careful monitor the key metrics moving forward: Revenue, carrier relationships, carrier concentration, operating income, balance sheet, and net income. PN has a competitive moat as a low cost provider, high switching costs, and outstanding management. It is our expectation that this investment would double in 12 to 24 months. We look forward to strong gains from our ownership of PN.

Works Cited

1) *PN Annual Report - SEC Filing 10-K.* EDGAR, 2014.